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Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF SECRETARY

In the Matter of)
)
Federal-State Joint Board on) CC Docket No. 96-45
Universal Service)
)

REPLY COMMENTS

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Teleport Communications Group Inc. ("TCG") hereby offers the following reply to the initial comments filed in the Commission's Notice of Proposed Rulemaking in the above-captioned proceeding. In addition to addressing issues raised by others, TCG reiterates its recommendation that the Commission initiate a "Phase II" of this proceeding to investigate advanced universal services for schools, libraries, and rural health care providers. The volume of the initial comments indicates substantial interest in these topics, and a Phase II would permit all parties to devote the proper attention to these complex and important issues.

I. INTRODUCTION

The Telecommunications Act of 1996 ("Act") provides specific parameters for the development of a universal service mechanism:

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explicit support, funded in an equitable and non-discriminatory manner by all interstate telecommunications carriers, and available to all eligible carriers. Despite the clarity of these parameters, a number of parties have used this opportunity to propose programs or actions that do not meet these requirements. TCG urges the Commission to maintain its focus on implementing the intent and letter of the Act, and on providing much-needed guidance to the states in the development of their own universal service mechanisms.

II. DISCUSSION

A. Rate Rebalancing and Pricing Flexibility

A number of parties have suggested that universal service would be enhanced via "rate rebalancing" or "pricing flexibility."¹ This issue does not belong in this proceeding for two reasons. First, rate rebalancing leads to increased rates for the monopoly's captive customers and lower rates for those customers most likely to have a choice of providers. Raising rates in the name of universal service strikes TCG as ironic at best and counter-productive at worst, particularly

¹See, e.g., Comments of Southwestern Bell at 3-4, US West at 3, USTA at 15.

given that it has not even been determined that rates are below cost. Similarly, granting pricing flexibility to monopoly local exchange carriers far in advance of the development of effective competition would only tighten the monopolist's grip on its captive customers. Full and effective competition will be the ultimate guarantor of universal telephone service. Additionally, nothing in the Act mandates that the Commission's consideration of universal service must (or should) encompass major rate changes in local retail rates. Suggestions that the Commission take up those complex and contentious issues here can only lead to unnecessary delays and confusion in this proceeding. A properly structured, competitively-neutral universal service program like the one envisaged by the Act and proposed by TCG -- rather than "rate rebalancing" and "pricing flexibility" -- will ensure that rates for basic service will remain affordable at current levels.

B. Carrier Common Line Charges

Some parties suggest that the Carrier Common Line Charge ("CCLC") is an implicit subsidy of basic service and therefore is inconsistent with the Act.² To remedy this perceived

²See, e.g., Comments of USTA at 15, Southwestern Bell at 4, Ameritech at 21, and BellSouth at 10

inconsistency, these parties have proposed recovering those costs from the universal service mechanism or from the subscriber line charge ("SLC").

These contentions are incorrect. The CCLC, like the SLC, is simply a means of recovering the costs of that portion of the local loop allocated to the interstate jurisdiction.³ Going back as far as *Smith v. Illinois Bell*, it has been long recognized that the local loop supports interstate services and accordingly a portion of its costs can be properly recovered from an interstate charge. In that regard, the CCLC and SLC are really no different than intrastate local exchange charges, in that all of them are simply tariff mechanisms to recover the costs of providing local service from the users of those services. The idea that the Commission should now recover these interstate costs from the universal service mechanism is far beyond the intent of the statute, and would unnecessarily increase the burden on contributors to the fund.

C. Historic Costs

Both Southwestern Bell and US West have proposed that incumbent local exchange carriers should be allowed to recover

³See Comments of TCG at 10-11.

the "historic costs" of providing universal service.⁴ The Commission must categorically reject this suggestion. Contrary to US West's assertion that the emergence of competition "displaces many historical support mechanisms,"⁵ those states that have investigated universal service have concluded otherwise. In Washington, the Utilities and Transportation Commission found that:

".. it will be some time before new entrants have any genuine effect on the revenues of the incumbent LECs... Previous experiences with telecommunications competition have shown that market shares change slowly even when changing providers is relatively easy for consumers, as is the case in the long distance services market. Moreover, it will be difficult for customers to change local exchange providers in the near future. Most will not even have the option, because networks take time to construct."⁶

Southwestern Bell, whose hostility to competition is well known, goes so far as to suggest that the Act "requires that rates be adjusted to eliminate this prospective source (undepreciated

⁴See, e.g., Comments of Southwestern Bell at 23, US West at 4.

⁵Comments of US West at 4.

⁶WUTC, Fourth Supplemental Order Rejecting Tariff Filings and Ordering Refiling; Granting Complaints, in Part, Docket No. UT-941464, Docket No. UT-941465, Docket No. UT-950146, Docket No. UT-950265 (October 31, 1995).

investment) of implicit universal service support funding.⁷ Undepreciated investment recovered via rates from still-captive customers can hardly be construed as an implicit universal service subsidy that now warrants recovery from the revenues of other carriers. TCG encourages the Commission to state clearly and unequivocally that recovery of prior investment is not an implicit subsidy covered by the Act and that the LECs' ability to recover their investment will not be hindered by the development of competition.

D. "Play-or-Pay" and The Act

Competition will ultimately reduce, if not eliminate entirely, the need for any external universal service support, as suggested by Southern New England Telephone.⁸ Nevertheless, to the extent that a universal service mechanism is required as competition develops, it must conform to the parameters established by the Act: explicit support, funded by all interstate telecommunications providers, and available to all eligible carriers. The so-called "play-or-pay" scheme that has

⁷Comments of Southwestern Bell at 23 n. 36.

⁸Comments of Southern New England Telephone at 5.

been adopted in New York and advocated by NYNEX⁹ clearly violates the Act's parameters for a universal service mechanism, as well as its cost standards for reciprocal compensation¹⁰. TCG therefore urges the Commission to reject "play-or-pay" and any other mechanism that links universal service obligations with rate structures for reciprocal compensation. TCG requests that the Commission find that "play-or-pay" approaches do not conform to the requirements of the Act and thus cannot be used for federal or state universal service purposes.

E. Resale of Basic Service and Universal Service Support

The Commission needs to consider the implications for universal service, as well as the impact on facilities-based competition, of the wholesale pricing requirements of the Act, which mandates that wholesale service be provided at retail rates less "avoided costs"..¹¹ By definition, universal service support should be available to those customers for whom the cost of service exceeds the affordable rate. A discount from that rate will only increase the difference between the cost and the

⁹Comments of NYNEX at 15.

¹⁰Sec. 252(d)(2).

¹¹Sec. 252(d)(3).

rate. Of far greater importance, however, is which carrier should receive the support from the universal service mechanism: the wholesaler or the reseller? Clearly, if the reseller were to purchase the resold service at cost, then it would be reasonable for the reseller to collect the support. On the other hand, if the reseller were to purchase the service at something less than cost, then the wholesaler should collect the support. If the reseller were to collect the universal service support even if it purchased the service at a rate below cost, then the facilities-based wholesaler would be unable to recover its own costs. TCG urges the Commission, therefore, to ensure that its rules for universal service reflect these scenarios. That is, universal service support should flow to the reseller when the reseller pays the facilities-based carrier the full cost of the service; conversely, the facilities-based carrier should receive the support when it sells the service at less than cost.

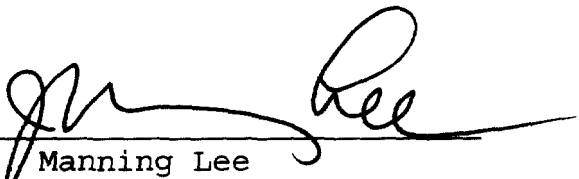
III. CONCLUSION

The establishment of an explicit universal service fund, supported by all interstate carriers, and available to all eligible carriers, is fundamental to the Act's goals of advancing universal service in a competitively-neutral manner. Proposals

that would impose rate increases on captive customers or that award pricing flexibility to monopolists will only frustrate the achievement of those goals. Furthermore, the Commission should issue unequivocal rules that would prohibit the continuation of implicit subsidies via "play-or-pay" schemes that clearly violate both the universal service and reciprocal compensation provisions of the Act. Finally, the resale of basic service requires special rules to ensure that the carrier that bears the cost of providing universal service is appropriately compensated from the universal service fund.

Respectfully submitted,

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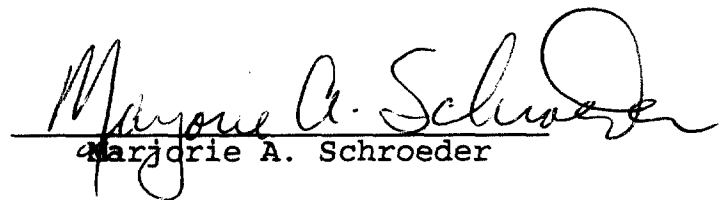
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